

Research on State Responsibility Issues in the Application of Legitimacy Clauses in Corrupt Situations

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Abstract

In international investment arbitration involving corruption, host country often invoke legality clauses, leading tribunals to decline jurisdiction or find the claim inadmissible. This leaves investors solely bearing the adverse consequences. Such an outcome reflects an "Attribution Asymmetry": tribunals improperly overlook the host country's own share of liability. Under the Draft Articles on Responsibility of States for Internationally Wrongful Acts (hereinafter "Articles on State Responsibility"), adopted by the International Law Commission at its fifty-third session in 2001, corruption is attributable to the state and constitutes an internationally wrongful act. Consequently, the host country should bear responsibility jointly with the investor for the corrupt conduct.

Keywords

International Investment Arbitration, Corruption, Legality Clauses, Bilateral Investment Treaties, State Responsibility.

1. Introduction

Nowadays, many countries suppress corrupt investments through the "legitimacy clauses" in bilateral investment treaties (BITs) in order to reduce corruption in international investment and promote sustainable investment development. But in cases where investment involves corruption, the application of the "legitimacy clause" may have some additional negative effects. For example, when investors involved in corruption file claims with the International Centre for Settlement of Investment Disputes (ICSID), the host country often cites the legality clause to raise objections, and the arbitral tribunal often refuses jurisdiction or considers the case to be inadmissible as a result. At this point, regardless of whether the responsibility for corruption lies with the investor or the host country, it often leads to the investor bearing the adverse consequences arising from corruption. In this situation, there is still controversy in both theoretical and practical circles over whether the host country should bear national responsibility for corrupt behavior arising from regulatory deficiencies and weaknesses in the host country in an investment involving corruption.

On the basis of analyzing the consequences of the application of legality clauses in cases involving corruption, this article will attempt to explore the issue of host country state responsibility in investments involving corruption from the perspective of the International Law Commission's "Draft Articles on Responsibility of States for Internationally Wrongful Acts" (hereinafter referred to as the "Articles on State Responsibility").

2. The consequences of the application of legality clauses in cases involving corruption: Attribution Asymmetry

With the increasing focus on non-investment interests beyond investment in the international investment field, the protection of regulatory rights in host countries has attracted much attention, which has also led to the protection of regulatory rights in host countries being listed

as a general goal of all international investment agreements, just like the protection of the rights of foreign investors [1]. The legality clause refers to the content established in BITs to protect the regulatory rights of the host country, with the goal of balancing the interests of investors and the regulatory rights of the host country, in order to protect both. However, when investments involving corruption violate the legality clause, the application of the legality clause may lead to an unequal distribution of responsibilities between investors and the host country, thereby deviating from the original intention of establishing the legality clause.

Since the *Salini v. Morocco* arbitration tribunal established "compliance with the laws of the host country" as a requirement for the legality of investments [2], the legality clause in BITs has gradually become an essential element that cannot be ignored by the arbitration tribunal. Afterwards, many arbitration tribunals followed the ruling approach of the arbitral tribunal in this case. The arbitral tribunal in the *Bayindir v. Pakistan* case [3] cited the interpretation and application of the legality clause in the *Salini* case in its case law documents. Furthermore, some arbitral tribunals have held that investments that violate the legality clause can be dismissed by the tribunal on the grounds of lack of jurisdiction or inadmissibility, as in the case of *Anderson v. Costa Rica* [4].

Moreover, corruption is considered a crime that infringes upon the regulatory authority of the host country in most countries. Therefore, in investment arbitration involving corruption, it can also lead to the application of legality clauses. However, in such cases, the host country often violates the legality clause by claiming corrupt means such as bribery used by investors in the process of obtaining or maintaining investment opportunities, which leads to the arbitral tribunal refusing jurisdiction over the case or considering the case unacceptable. In cases such as *Inceysa v. Salvador* [5], *Metal Tech v. Uzbekistan* [6], etc., the arbitral tribunal found that it had no jurisdiction over the case because the investor's behavior involved corruption and violated the relevant regulations of the host country.

In investment arbitration cases involving corruption published by ICSID, only the investor bears the risks and responsibilities arising from corrupt behavior, losing the right to obtain remedies, while the host country has hardly received any substantive or procedural punishment. This makes it possible for the host country to escape legal responsibility when it violates its obligations under international investment treaties through the use of legitimacy clauses. In the context of corruption, the application of legitimacy clauses unilaterally benefits the host country, leading to unequal distribution of responsibilities between investors and the host country.

Scholars have described the unfair outcomes resulting from the application of legality clauses by the arbitral tribunal as "Attribution Asymmetry" [7], believing that this is an improper disregard of the responsibility of the arbitral tribunal towards the host country. In practice, in addition to the situation where investors actively bribe officials of the host country government, there are also widespread cases where officials of the host country government actively solicit bribes from investors. However, within the framework of legitimacy clauses, even if the host country government officials actively solicit bribes from investors, once the investors agree to such bribery and bribe them, the responsibility for such corrupt behavior will be exempted from the host country and its government officials. This situation may lead to the host country actually tolerating or participating in corrupt behavior, seriously undermining the fairness of international investment activities.

It can be seen that when the legality clause is applied in cases involving corruption, when it comes to attribution issues, not only should the responsibility of investors be considered, but also the responsibility of the host country and its government officials should be taken into account. Due to the fact that corrupt practices are often directly involved by government officials of the host country, rather than by the host country as a whole, therefore, when

discussing the responsibilities of the host country and its government officials, the state responsibility of the host country must be taken into account.

3. State responsibility in investments involving corrupt practices

There is almost no dispute that investors bear responsibility in an investment involving corruption. However, corruption is not only the crime of bribe givers, but also the crime of state officials who accept or solicit bribes. Under the requirements of international anti-corruption conventions and BITs, host countries have the obligation to eliminate domestic corruption and protect investors, and should strictly regulate the behavior of government officials to prevent the occurrence of corruption. There is still controversy in both theoretical and practical circles regarding whether the host country should bear state responsibility for corrupt practices arising from the lack and weakness of regulation in the host country. The consensus reached so far is that the International Law Commission's "Articles on State Responsibility" will serve as an important reference for this issue. The "Articles on State Responsibility" are applicable to resolving all forms of international disputes, and international investment arbitration often uses the "Articles on State Responsibility" as a basis for judgment [8]. This section of this article will discuss whether the corrupt behavior of government officials in the host country constitutes an internationally wrongful act of the host country under the normative basis of the "Articles on State Responsibility", and whether the host country needs to bear state responsibility for this internationally wrongful act. Due to Article 2 of the "Articles on State Responsibility", in order to determine whether a state's conduct constitutes an internationally wrongful act, it is necessary to simultaneously satisfy the two basic elements of "(a) attributable to the state under international law" and "(b) the conduct violates the state's international obligations". Therefore, the discussion in this section will be conducted from these two parts in sequence.

3.1. Whether corrupt behavior can be attributed to the state or not

Attributing corrupt behavior of host country officials to the state is the primary condition for the host country to assume state responsibility. The corrupt behavior of these government officials is often personal and likely to be beyond their authority. How to view the connection between the actions of individuals who exceed their authority and the state, needs to consider that the state is actually an abstract legal entity, and its intangible existence determines that it can only operate through tangible actions of individuals and entities representing it, and these actions are inevitably regarded as the actions of the state itself, even if they conflict with the internal norms of the entity. Just as the principle of agency in all countries' legal systems requires companies to take responsibility for the actions of their employees (which may exceed their agency authority), countries are also responsible for the actions of their representatives that violate international obligations. The provisions of Articles 4 and 5 of the "Articles on State Responsibility" provide a legal basis for officials' personal actions to be considered as acts of the state [9]. And, Article 7 of the "Articles on State Responsibility" affirms that, the possibility of an individual exceeding their authority or violating instructions leading to state responsibility [10].

At this point, there seems to be no theoretical barrier to attributing the corrupt behavior of government officials in the host country to the state, but before drawing this conclusion, we also need to pay attention to the attribution premise of "acts in that capacity" in Article 7 of the "Articles on State Responsibility". The International Law Commission explained the specific content of this premise in its commentary as follows: "Although case law has always held that acts of exceeding authority should be held responsible, it is necessary to distinguish these acts from those of public officials that go far beyond their official functions, as these acts should be considered private acts." Early versions of the "Articles on State Responsibility" also elaborated

on this article: the reporter Roberto Ago pointed out in Article 10 (2) of the "Articles on State Responsibility": "If such acts are fundamentally beyond the specific functions of the organ, or even if from other aspects, the organ clearly lacks authority, they are not considered acts of the State." [11] This article argues that soliciting or accepting bribes is clearly not an official function of the host country government officials, nor does it belong to their actual authority, but their subsequent actions in seeking benefits for investors (whether legitimate or illegitimate) are often closely related to the authority and status of government officials. Whether it is the active bribery of investors or the active solicitation of bribes by host country government officials, the ultimate realization of corrupt activities refers to the actions or inactions of government officials in their official capacity, in order for investors who pay bribes to obtain investment opportunities.

We can also understand the inevitability of host country officials "acts in that capacity" from the special nature of corrupt behavior. Corruption is not solely composed of investors bribing officials in the host country, or officials seeking personal or others' personal gain, but rather a combination of officials' private and official actions. The crimes involved in a corrupt act can be divided into multiple charges in international anti-corruption conventions and domestic laws of various countries, such as the crime of accepting bribes, the crime of offering bribes, the crime of abuse of power, and the crime of perverting the course of justice for private ends. Overall, corrupt practices in international investment can be divided into two stages: the first stage involves investors bribing government officials in the host country, who accept bribes based on personal interests; in the second stage, after accepting bribes, officials act in their official capacity and carry out or refrain from carrying out an act (which may be completely legal or beyond their official authority) in exchange for benefits for investors. In the first stage, whether it is officials extorting money or other property benefits from investors, or passively accepting bribes, such behavior completely exceeds the specific authority of the official and their agency, and therefore cannot be considered official behavior. This is easy to understand. If the act of receiving benefits is carried out by state organs or individuals representing state organs, then bribery actually does not exist and should be defined as an administrative act of state organs. In the second stage, host country officials, as the main body exercising public power, are clearly attempting to use their official power to seek benefits for investors. Despite having private intentions, their behavior is manifested in an official capacity. Regardless of whether the act of seeking benefits for others exceeds their authority, whether the benefits sought for others are legitimate, and whether the benefits sought for others are realized, officials are acting in an official capacity. This is also confirmed in the footnote of the commentary to Article 7 of the "Articles on State Responsibility": "An ultra vires act covered by Article 7 is when a state official accepts bribes to carry out an act or enter into a transaction. [12]" From this, it can be seen that the International Law Commission holds a positive attitude towards the attribution of corruption by officials of the host country to the state.

3.2. Whether the host country violated its international obligations or not

As Judge Higgins pointed out, "the fact that the institution is a derivative of the state is sufficient in itself, and there is no need to prove any fault or malice on the part of the state." [13] However, in determining whether a state should be held responsible for the actions of individuals or entities, another fundamental element of international responsibility should also be considered, that is, the existence of a breach of international obligations by the state. Before discussing this issue, it is necessary to first clarify the scope of international obligations that the host country needs to undertake. The "Articles on State Responsibility" provide the widest interpretation of the scope of international obligations that a state may violate in its commentary, which may be established by a customary rule of international law, by a treaty or by a general principle applicable within the international legal order, [14] and can involve relatively minor

infringements as well as the most serious breaches of obligations under peremptory norms of general international law. [15] The corruption governance provisions in the international investment corruption governance treaties or international investment agreements concluded or participated in by the host country government constitute the main international legal basis for the governance of international investment corruption. The attitude of international law towards corrupt practices in international investment has gone through a process from *laissez faire* or even supportive to criminalizing investor behavior, and then to punishing both investors and host country officials simultaneously. The international community's regulation of corruption can be traced back to the 1969 Vienna Convention on the Law of Treaties. Article 50 of the Convention stipulates: "If the expression of a State's consent to be bound by a treaty has been procured through the corruption of its representative directly or indirectly by another negotiating State, the State may invoke such corruption as invalidating its consent to be bound by the treaty." This article for the first time developed the contract law rule of invalidity of contracts obtained through corruption into an anti-corruption rule in international law. The Convention on Combating Bribery of OECD Legal Instruments Foreign Public Officials in International Business Transactions is the first global anti-corruption convention signed between developed countries in 1997. In 2003, the United Nations adopted the United Nations Convention against Corruption, aiming to provide a comprehensive anti-corruption framework for the international community. This convention requires countries to classify "when committed intentionally, the promise, offering or giving to a foreign public official or an official of a public international organization, directly or indirectly, of an undue advantage, for the official himself or herself or another person or entity, in order that the official act or refrain from acting in the exercise of his or her official duties, in order to obtain or retain business or other undue advantage in relation to the conduct of international business" and "when committed intentionally, the solicitation or acceptance by a foreign public official or an official of a public international organization, directly or indirectly, of an undue advantage, for the official himself or herself or another person or entity, in order that the official act or refrain from acting in the exercise of his or her official duties" as criminal offenses. [16] In addition, this convention requires contracting states to enact laws and other measures to prevent "the embezzlement, misappropriation or other diversion by a public official for his or her benefit or for the benefit of another person or entity, of any property, public or private funds or securities or any other thing of value entrusted to the public official by virtue of his or her position" [17] and "the abuse of functions or position, that is, the performance of or failure to perform an act, in violation of laws, by a public official in the discharge of his or her functions, for the purpose of obtaining an undue advantage for himself or herself or for another person or entity" [18]. The relevant provisions of such anti-corruption conventions or documents, in addition to regulating the "supply" side of bribery, namely bribe givers or bribe providers (inevitably investors), also focus on the "demand" side of bribery on the other side of the equation, namely the host country government officials who accept bribes. It cannot be denied that since the international community has defined transnational corruption as a crime, as the main body of various anti-corruption conventions, countries have an absolute responsibility to combat corruption in international investment. This responsibility is not based on causing any kind of harm, nor is it only borne by one party in international relations, but rather shifts from a purely inter state nature to a responsibility towards the entire international community [19].

Overall, we can draw a conclusion. Whether the host country officials actively solicit bribes or passively accept them, and whether their official actions exceed their authority, such behavior can be attributed to the state. Moreover, the state has an obligation under international law to combat corruption. The host country's inadequate supervision of officials' involvement in corruption and the prevalent corrupt investment environment in the country undoubtedly violate this responsibility. Therefore, in an international investment involving corruption, the

host country is not innocent and should bear the state responsibility stipulated in the "Articles on State Responsibility". It should be emphasized that focusing on the assumption of national responsibility in the context of corrupt investment is not to achieve the consequences of the host country compensating investors for corrupt behavior, which is obviously unreasonable. What investors truly claim compensation for is the losses caused to investors by other actions of the host country. The assumption of state responsibility is more of a defense by investors against corruption in the host country, in order to ensure that they can obtain protection from the arbitration tribunal.

4. Conclusion

In arbitration involving investment corruption, the application of legality clauses should not only make investors the sole bearers of responsibility. A more reasonable way is to comply with the original intention of legality clauses, balance the interests of investors and the regulatory rights of the host country, and achieve common protection for both parties. This also means that in arbitration of investment activities involving corrupt practices, both investors and the host country should have the legal possibility of becoming responsible for adverse consequences.

Due to the fact that corruption in investment activities is often directly involved by investors and government officials of the host country, according to the analysis in this article, the suspected corrupt behavior of government officials of the host country in investment activities can be attributed to the host country. Therefore, this article believes that the host country can also become the responsible party for corrupt practices in investment activities.

Due to limited space, this article did not delve into the issues such as specific attribution methods between investors and host countries, reasonable limitations of legality clauses, standards for proof of liability, and how to determine specific compensation amounts, etc. For these issues, further research and exploration will be needed.

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